Appendix B

Annual Treasury Management Report (Incorporating Outturn Prudential Indicators)

2021/22

Breckland Council
June 2022

1 Introduction and Background

1.1 This report summarises the following:-

- Capital activity during the year;
- Impact of this activity on the Council's underlying indebtedness, (the Capital Financing Requirement);
- The actual prudential and treasury indicators;
- Overall treasury position identifying how the Council has borrowed in relation to this indebtedness, and the impact on investment balances;
- Summary of interest rate movements in the year;
- Detailed debt activity; and
- Detailed investment activity.

2 The Council's Capital Expenditure and Financing

2.1 The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

£m General Fund	31.3.21 Actual	2021/22 Budget	31.3.22 Actual
Capital expenditure	**7.246**	**8.622**	**6.613**
Financed in year: Capital reserves Revenue Funding PFI Scheme Capital Grants and S106 Agreements	 3.605 0.219 0.628 2.794		 1.674 1.175 0.152 2.917
Unfinanced capital expenditure	**0**		**695**

3 The Council's Overall Borrowing Need and Related Prudential Indicators

3.1 The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2021/22 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

3.2 Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies, (such as the Government, through the Public Works Loan Board [PWLB], or the money markets), or utilising temporary cash resources within the Council. The Council had a positive CFR in 2021/22 and so had an underlying need to borrow for a capital purpose.

3.3 Reducing the CFR – the Council's underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision – MRP, to reduce the CFR. This is effectively a repayment of the General Revenue Account borrowing need. This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR. In accordance with regulations, MRP does not have to be charged in a year when the CFR was negative at the end of the previous financial year.

3.4 The total CFR can also be reduced by:

- the application of additional capital financing resources, (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

3.5 The Council's 2021/22 MRP Policy, (as required by DLUHC Guidance), was approved by Full Council as part of the Treasury Management Strategy Report for 2021/22 on 20th January 2021.

3.6 The Council's CFR for the year is shown below, and represents a key prudential indicator. It includes PFI and leasing schemes on the balance sheet, which increase the Council's borrowing need. No borrowing is actually required against these schemes as a borrowing facility is included in the contract. The Council has complied with this prudential indicator.

CFR (£m): General Fund	31.3.21 Actual	2021/22 Budget	31.3.22 Actual
Opening balance	7,557	11,117	7,557
Add unfinanced capital expenditure (as above)	0	(1,279)	695
Less MRP	0	(539)	(539)
Less PFI & finance lease repayments	(7,780)	(7,780)	(7,511)
Closing balance	**(223)**	**1,519**	**202**

Borrowing activity is constrained by prudential indicators for gross borrowing and the CFR, and by the authorised limit.

Gross borrowing and the CFR - in order to ensure that borrowing levels are prudent over the medium term and only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2021/22) plus the estimates of any additional capital financing requirement for the current (2022/23) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator would allow the Council some flexibility to borrow in advance of its immediate capital needs if required. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

	31.3.21 Actual	2021/22 Budget	31.3.22 Actual
Gross borrowing position	£0.00m	£0.00m	£0.00m
CFR	(£0.223m)	£1.519m	£0.202m
Under / (over) funding of CFR	(£0.223m)	£1.519m	£0.202m

The authorised limit - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. The table below demonstrates that during 2021/22 the Council has maintained gross borrowing within its authorised limit.

The operational boundary – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary are acceptable subject to the authorised limit not being breached.

Actual financing costs as a proportion of net revenue stream - this indicator identifies the trend in the cost of capital, (borrowing and other long term obligation costs net of investment income), against the net revenue stream. Financing costs to net revenue stream are negative for 2021/22, this is because the Council is earning interest on its balances as opposed to paying interest on its borrowing.

	2021/22

Authorised limit	£9.511m
Maximum gross borrowing position during the year	£0.0m
Operational boundary	£7.511m
Average gross borrowing position	£0.0m
Financing costs as a proportion of net revenue stream	(0.71%)

4 Treasury Position as at 31st March 2022

4.1 The Council's treasury management debt and investment position is organised by the treasury management service in order to ensure adequate liquidity for revenue and capital activities, security for investments and to manage risks within all treasury management activities. Procedures and controls to achieve these objectives are well established both through member reporting detailed in the summary, and through officer activity detailed in the Council's Treasury Management Practices. At the end of 2021/22 the Council's treasury, (excluding borrowing by PFI and finance leases), position was as follows:

DEBT PORTFOLIO	31.3.21 Principal	Rate/ Return	Average Life yrs	31.3.22 Principal	Rate/ Return	Average Life yrs
Fixed rate funding:						
-PWLB	£0.00m	N.a.		£0.00m	N.a.	
-Market	£0.00m	N.a.		£0.00m	N.a.	
Variable rate funding:						
-PWLB	£0.00m	N.a.		£0.00m	N.a.	
-Market	£0.00m	N.a.		£0.00m	N.a.	
Total debt	**£0.00m**	**N.a.**	**N.a.**	**£0.00m**	**N.a.**	**N.a.**
CFR	**(£0.223m)**			**£0.202m**		
Over / (under) borrowing	**£0.223m**			**(£0.202m)**		
Total investments	**£27.398m**	**0.28%**		**£40.562m**	**0.29%**	

INVESTMENT PORTFOLIO	31.3.21 Actual £000	31.3.21 Actual %	31.3.22 Actual £000	31.3.22 Actual %
Treasury investments				
Banks	13,398	48.90%	23,562	58.09%
Building Societies - rated	7,000	25.55%	15,000	36.98%
Local authorities	7,000	25.55%	0	
DMADF (H M Treasury)	0		2,000	4.93%
Total managed in house	27,398	100%	40,562	100%
Bond funds	0		0	
Property funds	0		0	
Cash fund managers	0		0	
Total managed externally	0		0	
TOTAL TREASURY INVESTMENTS	27,398	100%	40,562	100%

Non Treasury investments				
Loans to Breckland Bridge	270		270	
TOTAL NON TREASURY INVESTMENTS	270	100%	270	100%

Treasury investments	27,398	99.02%	40,562	99.34%
Non Treasury investments	270	0.98%	270	0.66%
TOTAL OF ALL INVESTMENTS	27,668	100%	40,832	100%

The maturity structure of the investment portfolio was as follows:

	31.3.21 Actual £000	**31.3.22 Actual £000**
Investments		
Longer than 1 year	270	270
Up to 1 year	27,398	40,562
Total	27,668	40,832

5.1 Investment strategy and control of interest rate risk

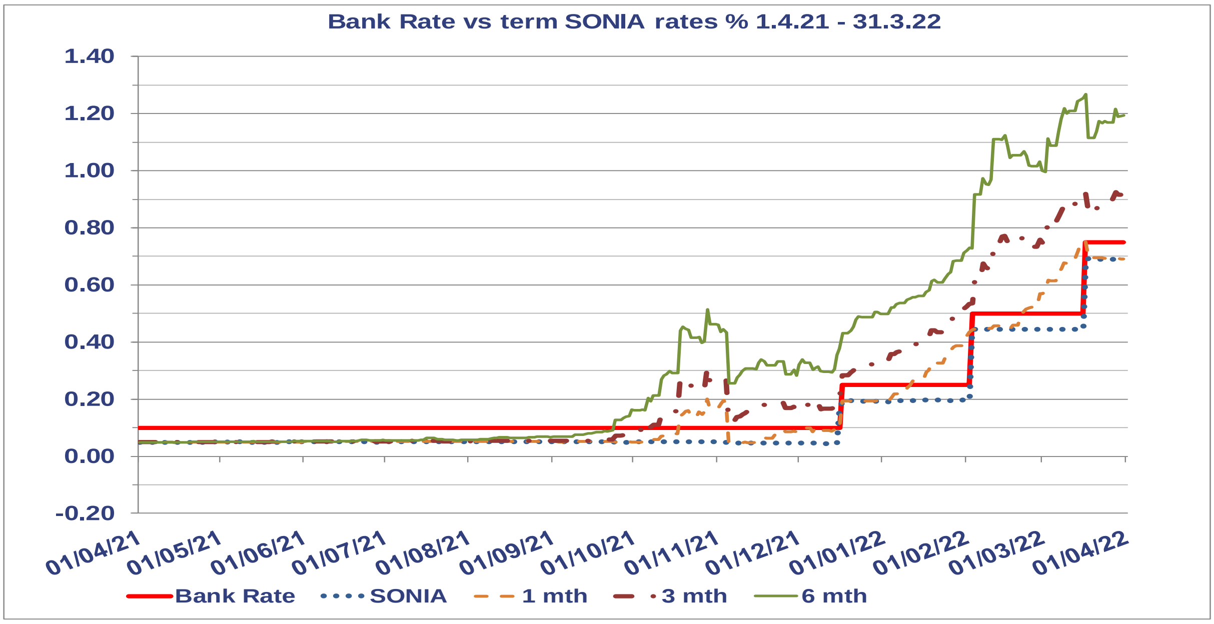
5.1.1 There were no changes to the Strategy during 2021/22. Investment returns remained close to zero for much of 2021/22. Most local authority lending managed to avoid negative rates and one feature of the year was the continued growth of inter local authority lending. The expectation for interest rates within the treasury management strategy for 2021/22 was that Bank Rate would remain at 0.1% until it was clear to the Bank of England that the emergency level of rates introduced at the start of the Covid-19 pandemic was no longer required.

5.1.2 The Bank of England and the Government also maintained various monetary and fiscal measures, supplying the banking system and the economy with massive amounts of cheap credit so that banks could help cash-starved businesses to survive the various lockdowns/negative impact on their cashflow. The Government also supplied huge amounts of finance to local authorities to pass on to businesses. This meant that for most of the year there was much more liquidity in financial markets than there was demand to borrow, with the consequent effect that investment earnings rates remained low until towards the turn of the year when inflation concerns indicated central banks, not just the Bank of England, would need to lift interest rates to combat the second-round effects of growing levels of inflation (CPI rose to 6.2% by March 2022).

5.1.3 While the Council has taken a cautious approach to investing, it is also fully appreciative of changes to regulatory requirements for financial institutions in terms of additional capital and liquidity that came about in the aftermath of the financial crisis. These requirements have provided a far stronger basis for financial institutions, with annual stress tests by regulators evidencing how institutions are now far more able to cope with extreme stressed market and economic conditions.

5.1.4 Actual changes in interest rates and in the SONIA benchmark rate are shown in the graph and table below.

Investment Benchmarking Data – Sterling Overnight Index Average 2021/22



	Bank Rate	SONIA	1 mth	3 mth	6 mth
High	0.75	0.69	0.75	0.93	1.27
High Date	17/03/2022	18/03/2022	16/03/2022	28/03/2022	17/03/2022
Low	0.10	0.05	0.05	0.05	0.05
Low Date	01/04/2021	15/12/2021	10/11/2021	14/04/2021	09/04/2021
Average	0.19	0.14	0.17	0.24	0.34
Spread	0.65	0.65	0.71	0.88	1.22

5.2 Borrowing strategy and control of interest rate risk

5.2.1 During 2021/22, the Council maintained an under-borrowed position. This meant that the capital borrowing need, (the Capital Financing Requirement), was not fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow was used as an interim measure. This strategy was prudent as investment returns were very low and minimising counterparty risk on placing investments also needed to be considered.

5.2.2 A cost of carry remained during the year on any new long-term borrowing that was not immediately used to finance capital expenditure, as it would have caused a temporary increase in cash balances; this would have incurred a revenue cost – the difference between (higher) borrowing costs and (lower) investment returns.

5.2.3 The policy of avoiding new borrowing by running down spare cash balances has served well over the last few years. However, this was kept under review to avoid incurring higher borrowing costs in the future when this authority may not be able to avoid new borrowing to finance capital expenditure.

5.2.4 Against this background and the risks within the economic forecast, caution was adopted with the treasury operations. The Assistant Director Finance therefore monitored interest rates in financial markets and adopted a pragmatic strategy based upon the following principles to manage interest rate risks.

- if it had been felt that there was a significant risk of a sharp FALL in long and short term rates, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then long term borrowings would have been postponed, and potential rescheduling from fixed rate funding into short term borrowing would have been considered.

- if it had been felt that there was a significant risk of a much sharper RISE in long and short term rates than initially expected, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would have been re-appraised. Most likely, fixed rate funding would have been drawn whilst interest rates were lower than they were projected to be in the next few years.

5.2.5 Interest rate forecasts expected only gradual rises in medium and longer-term fixed borrowing rates during 2021/22 and the two subsequent financial years until the turn of the year, when inflation concerns increased significantly. Internal, variable, or short-term rates, were expected to be the cheaper form of borrowing until well in to the second half of 2021/22.

5.2.6 Forecasts at the time of approval of the treasury management strategy report for 2021/22 were as follows: -

Link Group Interest Rate View	9.11.20													
	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24
BANK RATE	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
3 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
6 month ave earnings	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
12 month ave earnings	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
5 yr PWLB	1.80	1.80	1.80	1.80	1.80	1.90	1.90	1.90	1.90	1.90	2.00	2.00	2.00	2.00
10 yr PWLB	2.10	2.10	2.10	2.10	2.20	2.20	2.20	2.30	2.30	2.30	2.30	2.30	2.30	2.30
25 yr PWLB	2.50	2.50	2.60	2.60	2.60	2.60	2.70	2.70	2.70	2.70	2.80	2.80	2.80	2.80
50 yr PWLB	2.30	2.30	2.40	2.40	2.40	2.40	2.50	2.50	2.50	2.50	2.60	2.60	2.60	2.60

5.2.7 No external borrowing was undertaken in 2021/22.

6 Investment Outturn

6.1 Investment Policy – the Council's investment policy is governed by DLUHC investment guidance, which has been implemented in the annual investment strategy approved by the Council on 20th January 2021. This policy sets out the approach for choosing investment counterparties, and is based on credit ratings provided by the three main credit rating agencies, supplemented by additional market data, (such as rating outlooks, credit default swaps, bank share prices etc.).

6.2 The investment activity during the year conformed to the approved strategy, and the Council had no liquidity difficulties.

6.3 Resources – the Council's cash balances comprise revenue and capital resources and cash flow monies. The Council's core cash resources comprised as follows:

Balance Sheet Resources (£m)	31.3.21	31.3.22
Balances	2.85	2.824
Earmarked reserves	25.234	18.812
Provisions	(2.462)	(2.272)
Usable capital receipts	0	0
Total	**25.622**	**19.364**

Earmarked reserves reduced over the year as one-off grant funding for Covid-19 NNDR reliefs that was held in reserves was repaid, since Breckland only retained 40% of this funding, which covered 100% of lost NNDR income.

6.4 **Investments held by the Council –** The Council managed all its investments internally.

- The Council maintained an average balance of £40.87m of internally managed funds, owing to one-off grants received for expenditure in later years.
- The internally managed funds earned an average rate of return of 0.2884%.
- The comparable performance indicator is the SONIA overnight rate, which was 0.14058%.
- This compares with a budget assumption of £11.5m investment balances earning an average rate of 2.61%.
- Total investment income was £127,190 compared to a budget of £235,666. This was due to delayed timing of loans to 3rd parties at market rates.

7 Performance Measurement

7.1 One of the key requirements in the Code is the formal introduction of performance measurement relating to investments, debt and capital financing activities. The Council's performance indicators were set out in the annual Treasury Management Strategy Statement.

7.2 This service has set the following performance indicators and operated within the boundaries set as detailed in the March performance report attached as Appendix C:

- **Security**
  Risk of default

- **Liquidity**
  Liquid short term deposits – The Council requires at least of £5m to be available with a month's notice.
  Weighted Average Life
  Bank Overdraft – The Council's approved overdraft facility is £2m

- **Yield**
  As LIBID ceased at 31 December 2021, we consulted with our advisors and determined that the SONIA overnight rate would be a suitable replacement benchmark.
  Actual interest earned against budget

Investment Portfolio

Treasury Investments held as at 31st March 2022:

Investment Type	Counterparty	Principal (£)	Start date	Maturity Date	Lowest Long Term Credit Rating
Call account	Barclays	£4,090,288.47	Call	Call	A
Call account	Handelsbanken	£3,472,000.00	Call	Call	AA-
Call account	Lloyds	£5,000,000.00	Call	Call	A+
Call account	Coventry Building Society	£5,000,000.00	Call	Call	A-
Fixed Term Deposit	SMBC Bank International	£2,000,000.00	04/03/2022	04/04/2022	A
Fixed Term Deposit	Yorkshire Building Society	£2,000,000.00	10/01/2022	11/04/2022	A-
Fixed Term Deposit	Nationwide Building Society	£1,000,000.00	17/01/2022	19/04/2022	A
Fixed Term Deposit	Goldman Sachs International Bank	£1,000,000.00	21/10/2021	21/04/2022	A+
Fixed Term Deposit	Nationwide Building Society	£2,000,000.00	25/10/2021	25/04/2022	A
Fixed Term Deposit	Yorkshire Building Society	£2,000,000.00	15/03/2022	03/05/2022	A-
Fixed Term Deposit	DMADF	£2,000,000.00	15/12/2021	16/05/2022	AA-
Fixed Term Deposit	Standard Chartered Bank	£2,000,000.00	21/01/2022	20/05/2022	A+
Fixed Term Deposit	Standard Chartered Bank	£1,000,000.00	22/02/2022	20/05/2022	A+
Fixed Term Deposit	Standard Chartered Bank	£1,000,000.00	21/02/2022	20/05/2022	A+
Fixed Term Deposit	Standard Chartered Bank	£2,000,000.00	23/02/2022	23/05/2022	A+
Fixed Term Deposit	Yorkshire Building Society	£1,000,000.00	15/03/2022	31/05/2022	A-
Fixed Term Deposit	Nationwide Building Society	£2,000,000.00	07/12/2021	07/06/2022	A
Fixed Term Deposit	Goldman Sachs International Bank	£2,000,000.00	04/01/2022	04/07/2022	A+
	Total Investments	**£40,562,288.47**			